Decision _____

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Application of Del Oro Water Co., Inc. (U-61-W) for a Determination by the Commission that Certain Main Extension Agreements between itself and Others are Neither Invalid nor Fail to Comply with the Utility's Rule 15 and/or the Commission's Decisions, Rules and Regulations Pertaining to Water Main Extension Agreements.	Application 00-11-053 (Filed November 20, 2000)

William G. Fleckles, Attorney at Law, for Del Oro Water Company, applicant.
Patrick J. Power and Morey W. Fuqua, Attorneys at Law, for Breuer, Inc., and Marshall S. Mayer, Attorney at Law, for Jacobs, Laney, and Kasza, protestants.
Marion Peleo, Attorney at Law, for the Water Branch of the Office of Ratepayer Advocates, intervenor.

O P I N I O N

1. Summary

Del Oro Water Company (Del Oro) seeks Commission resolution of a dispute over the validity of certain main extension agreements it entered into with developers and others in Del Oro's Lime Saddle District. This decision concurs with a staff analysis and audit and finds that the main extension agreements comply with the utility's tariffs and that Del Oro has properly accounted for funds collected through these agreements.

2. Procedural History

Del Oro filed this application after four Lime Saddle District customers brought suit against the utility in Butte County Superior Court. Plaintiffs contest the main extension agreements that Del Oro required them to sign beginning in 1991 in order to receive water service. Pursuant to Section A.8 of its Tariff Rule 15, Del Oro asked this Commission to rule on the validity of these main extension agreements. Section A.8 states:

> In case of disagreement or dispute regarding the application of any provision of this rule, or in circumstances where the application of this rule appears unreasonable to either party, the utility, applicant or applicants may refer the matter to the Commission for determination.

Protests to the application were filed by Breuer, Inc. (Breuer), a development corporation, and by two other developers and one couple, all of whom are the plaintiffs in the Superior Court lawsuits. The Superior Court consolidated these cases and granted a stay pending the Commission's consideration of this application.

The Commission conducted a prehearing conference on March 28, 2001, at which time it was determined that the Commission's Water Division was preparing an audit and a report on Del Oro's main extension agreements as part of a general rate case for the utility. A second prehearing conference was conducted on June 6, 2001, after the audit and staff report were issued. In a Scoping Memo issued on June 12, 2001, Assigned Commissioner Duque set dates for submission of written testimony and scheduled an evidentiary hearing for August 21-24, 2001. Commissioner Duque limited the scope of this proceeding to two issues:

1. Were the Main Extension Agreements in question issued in compliance with Tariff Rule 15 and the Commission's rules and regulations?

2. Have Del Oro Water Company and its Lime Saddle District properly accounted for funds collected through the Main Extension Agreements in question?

The hearing was conducted on August 21 and 22, 2001. Protestants elected not to present testimony and proceeded solely on cross-examination of applicant's two witnesses and the Water Division's two witnesses. The Water Division witnesses were represented at hearing by the Office of Ratepayer Advocates (ORA). Opening briefs were filed by Del Oro and by Breuer on October 24, 2001, and reply briefs were filed on November 7, 2001, at which time the matter was deemed submitted for Commission decision.

3. Summary of Dispute

The facts are not in dispute.

The water system serves the community of Paradise in Butte County. It previously was operated by the Lime Saddle Community Services District, a public entity not subject to the jurisdiction of this Commission. Because the district's five wells are inadequate to serve existing customers, the district purchased supplemental water from the Stirling Bluffs Corporation, a subsidiary of Del Oro. The purchased water was wheeled from Stirling Bluffs through the Paradise Irrigation District.

Del Oro in 1990 acquired the water system, including the district's right to an annual allotment of 200 acre-feet of water from Lake Oroville. Lake Oroville water was not available, however, because no facilities existed to bring it to Lime Saddle. Del Oro continued to purchase water under the agreement with Stirling Bluffs and Paradise Irrigation District.

The agreements with Stirling Bluffs and the irrigation district can each be terminated on five years' notice. Moreover, both Stirling Bluffs and the irrigation district can refuse to supply water if the needs of their own customers so require. Because of the uncertainty of the water supply, the Department of Health Services (DHS) limited the number of Lime Saddle District connections to a maximum of 440. At the time of acquisition by Del Oro, the district was serving 259 customers. DHS encouraged the district to devise a way to tap the Lake Oroville water.

In 1990, Del Oro retained engineers to design a project to interconnect the Lime Saddle system with Lake Oroville. The completed design envisioned a project that would replace the Stirling Bluffs water with Lake Oroville water and would permit the district to serve up to 861 connections. Cost of the project was estimated at $2.8 million.

Del Oro decided to finance the Lake Oroville project by imposing a $5,000 charge on each new residential connection. The charge was determined by dividing the required $2.8 million by the approximately 600 new customers that could be served with the new source of water. Beginning January 1, 1991, Del Oro imposed the charge on new customers through a water main extension agreement that Del Oro asserts is permitted by Rule 15, its water main extension tariff.

At hearing, Del Oro's president Robert Fortino testified that the company has imposed the fee on 19 new customers who requested approximately 190 connections. Breuer, which planned to construct 100 homes in the area, paid some $500,000, and other developers paid fees in the $100,000 range. According to the staff audit, Del Oro at the end of 1999 had collected $865,852 (before taxes, and not including interest) in contributions. Fortino testified that approximately $700,000 has been spent on Lake Oroville project facilities. These include a

1.5-million-gallon storage tank, 4,000 lineal feet of 10-inch transmission main, upgrades to a treatment plant, and land acquisition for planned booster stations. Fortino said that Del Oro plans to seek a low-interest state loan and to complete the Lake Oroville intertie in the near future.

4. Validity of Line Extension Agreements

Del Oro's Rule 15 deals with water main extensions to serve new customer connections in locations where the current water distribution system does not exist or is inadequate. In general, extensions of water mains to serve new customers are paid in advance by the customers and contributed to the utility. In some cases, the payment may be refunded in part if the new main extension is later used by other customers.

The Water Division, in its analysis, looked to two provisions of Rule 15:

Rule 15.C.1.b.

> If special facilities consisting of items not covered by Section C.1.a. are required for the service requested and, when such facilities to be installed will supply both the main extension and other parts of the utility's system, at least 50 percent of the design capacity (in gallons, gpm, or other appropriate units) is required to supply the main extension, the cost of such special facilities may be included in the advance, subject to refund, as hereinafter provided, along with refunds of the advance of the cost of the extension facilities described in Section C.1.a. above.

Rule 15.C.1.d.

> If, in the opinion of the utility it appears that a proposed main extension will not, within a reasonable period, develop sufficient revenue to make the extension self-supporting, or if for some other reason it appears to the utility that a main extension contract would place an excessive burden on customers, the utility may require nonrefundable contributions of plant facilities from developers in lieu of a main extension contract.

ORA witness Arthur B. Jarrett, program and project supervisor in the Water Division, concluded in his analysis that Del Oro's main extension agreement complied with Rule 15. He testified that a small water district like Lime Saddle was authorized under Rule 15.C.1.b. to prepare a standard main extension agreement covering "special facilities" like the Lake Oroville water intertie. Under 15.C.1.d., the utility also was authorized for good cause to require nonrefundable contributions as part of the standard main extension contract. Jarrett stated:

> "The [main extension] contracts are essentially identical, differing only in the information concerning property being served and the number of connections involved. The contracts contain the standard paragraphs with all the pertinent information required by the main extension rule, clearly stating the purpose for which the funds were to be used. The contracts also clearly state that the funds collected by Del Oro are to be contributed and not subject to refund. The contracts contain funding to cover the shared portion of the Lime Saddle Marina/Penz Intertie project without unfairly discriminating against any of the parties and without unfairly burdening existing customers with any costs." (Exhibit 15, at 3.)

Focusing on Rule 15.C.1.d., Breuer argues that the Lake Oroville intertie is not a "proposed main extension," that there is no showing that the proposed intertie will not be self-supporting, and that "contributions of plant facilities" cannot be interpreted to mean $5,000 cash contributions. It also faults the utility for adding non-tariff language to its main extension contract promising refunds, with interest, if the intertie project should subsequently be funded by a special assessment district. Testimony at hearing showed that Del Oro in 1995 sought formation of a special assessment district, but a majority of property owners opposed it.

Breuer argues that the $5,000 charge imposed by Del Oro in January 1991 was a "facilities fee," which this Commission did not authorize until April 1991 in Decision (D.) 91-04-068, a rulemaking proceeding. Breuer also contends that Del Oro breached its contract by starting work on the intertie project before adequate funds had been collected to (in the words of the main extension agreement) "commence and prosecute to completion" all of the work on the project. Since Del Oro served only 259 customers in 1991 and was authorized by the State to serve up to 181 additional connections, Breuer contends that it and other new customers could and should have been served without paying $5,000 per connection.

Del Oro responds that the $5,000 fee gave new customers the promise of an uninterruptible supply of water from Lake Oroville, as opposed to the current reliance on purchased water from entities free to cut off supply if those entities experience shortages. The utility notes that under the Commission's General Order 103, a water company is required to supply water "from a source reasonably adequate to provide a continuous supply of water." (General Order 103.II.1.b.1.b.)

Del Oro also argues that nothing in Rule 15 precludes a contribution of cash to be used to replace an unreliable source of water and that, in fact, Rule 15's provisions for refunds of advances contemplate cash transactions where a developer cannot itself install the required special facilities. As to the non-tariff language added to the contracts, Del Oro argues that promising refunds if alternative financing is arranged provides a benefit to protestants. Del Oro noted that the Water Division concluded that a provision like this that benefits customers did not conflict with the Commission's intent in enacting Rule 15.

4.1 Discussion

All parties agree that replacing the current interruptible supply of water with a reliable system for extracting Lake Oroville water is desirable for the customers of the Lime Saddle District. Where parties disagree is on the method of financing that replacement. Breuer maintains that it was unlawful for the utility to use Rule 15 line extension contracts to assess a fee of $5,000 on each new connection. Breuer correctly asserts that utility tariffs must be strictly construed. (*Transmix Corp.* v. *Southern Pacific Co.* (1960) 187 Cal.App.2d 257.) By parsing Rule 15.C.1.d. word by word, Breuer maintains that it has shown that the main extension contract violates the utility's tariffs.

Breuer, however, focuses exclusively on a single provision of Rule 15. It is axiomatic that a contract must be read as a whole. (Civ. Code § 1641.) So too must tariffs, which constitute a utility's contract with its customers. In enacting Rule 15.C.1.d., the Commission contemplated that non-refundable contributions would apply to "advance contracts" developed under Rule 15.C. and would apply to special facilities that would qualify as utility plant. The Commission stated:

> "Small utilities which would find it difficult to repay advance contracts out of net revenues should therefore require that the plant for these extensions be financed through non-refundable contributions from the developer." (D.82-01-062, 7 CPUC2d at 793.)

As the Water Division analysis asserts, Rule 15 contemplates water main extension agreements that include "special facilities" as well as mains. Obviously, connecting a new customer to a water system, particularly when the new customer intends to develop multiple housing units, will involve installation of pumps, additional storage capacity, fire hydrants, and other material besides the pipelines through which the water will flow. Because such

facilities vary widely from project to project, the Commission has declined to adopt a narrow definition of what constitutes a special facility. (*See* D.75205, adding the 50% language to Rule 15.C.1.b.; *see also* D.82-01-062, declining to exclude source and storage facilities as special facilities.)

Moreover, Rule 15 contemplates proportionate financing of special facilities similar to the proportionate financing in the Del Oro agreement. In D.82-01-062, Rule 15.C.2.c. was added to provide that "[w]henever costs of special facilities have been advanced…, the amount so advanced shall be divided by the number of lots (or living units, whichever is greater) which the special facilities are designed to serve, to obtain an average advance per lot (or living unit) for special facilities." (D.82-01-062, 7 CPUC2d 778, 806.)

Under the pre-1982 version of Rule 15, developers who paid for special facilities could look forward to progressive refunds of such expenditures. The 1982 rule gave small utilities like Del Oro's Lime Saddle District the ability to require applicants for new extensions to contribute funds for the work. (Rule 15.C.1.d.)

The main extension contract at issue here contains these elements. It covers special facilities (installation of a replacement source of water), proportionate financing (total cost divided by the number of new connections), and contribution of financing. As required by Rule 15, the contract sets forth the special facilities to be constructed. We agree with the Water Division that when Rule 15 and particularly Rule 15.C. are read as a whole, the main extension contract here is in compliance with the tariff. Rule 15.C.1.d. was not intended to be read alone, without regard to other provisions of Rule 15.C. Rather, Rule 15.C.1.d. was intended to be an alternative method of financing the main extensions and special facilities described in the tariff. We also agree with the Water Division that inclusion of a refund provision for developers if alternative

financing is arranged does not veer so far from the refund provisions of Rule 15 as to invalidate the contract.

We note that in April 1991, the Commission in D.91-04-068 authorized water utilities serving fewer than 2,000 connections to accept from individual customers amounts in contribution as "connection fees" covering actual costs of installing new connections and facilities. While that authority was not exercised here, its availability reflects the Commission's policy at the time of granting financial flexibility to small water companies seeking to upgrade their facilities.

Based on the record as a whole, we concur with the Water Division analysis and conclude that the main connection agreement at issue is in compliance with the utility's Rule 15 and the Commission's rules and regulations. Because our task here is merely to determine the validity of the contract at issue, we do not reach the question of whether the statute of limitations or the doctrine of laches serve as a bar to protestants' complaints.

5. Proper Accounting of Collected Funds

Testimony on whether Del Oro had properly accounted for funds collected through the main extension agreements was presented by James R. Wuehler, a certified public accountant and a utility financial examiner for the Commission. Wuehler examined bank records, general ledgers, and annual reports to the Commission for the funds collected. He reviewed canceled checks and invoices to verify expenditures of these funds. He conducted a field examination of the Lime Saddle District and its contracts and accounting for purchased water.

Wuehler testified that at the end of 1999, the Lime Saddle District had received $865,852 in main extension agreement contributions (not including interest), had paid $268,688 in income taxes on contributions, and had spent $678,412 on projects listed in the main extension agreements. He further found

that the funds collected were properly recorded and reported in the district's Account 132 (Special Accounts) and that the funds were deposited in a separate account with the Chico office of Paine Webber Inc. and, later, in a Bank of America savings account. Wuehler also found that the main extension agreements each state the purposes for which the funds were collected. He stated that his examination of canceled checks and invoices showed that the funds were used exclusively for those purposes.

After receipt of the audit report, Breuer stated that it would take no position on whether Del Oro had properly accounted for main extension agreement funds. Allegations of impropriety in the collection, use, and accounting of these funds had been raised initially by Marshall S. Mayer, the attorney for three of the protestants. At hearing, however, Mayer withdrew his written testimony, participating only to the extent of conducting cross-examination. Mayer has not filed briefs in support of his clients' protests.

Based on the staff audit report, and in the absence of any challenge to the conclusions of that report, we find that Del Oro and its Lime Saddle District have properly accounted for funds collected through the main extension agreements.

6. Change in Categorization

In Resolution ALJ 176-3052, dated December 17, 2000, the Commission preliminarily categorized this proceeding as ratesetting and preliminarily determined that no hearings were required. In his Scoping Memo of June 12, 2001, Assigned Commissioner Duque determined that hearings would be required. Our order today confirms the categorization of ratesetting but changes the determination to state that hearings were required.

7. Comments on Proposed Decision

The proposed decision of the Administrative Law Judge in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(d) and Rule 77.1 of the Rules of Practice and Procedure. Comments were received on _____.

Findings of Fact

1. Pursuant to Tariff Rule 15.A.8., Del Oro seeks a Commission ruling on the validity of a main extension agreement that the utility required for new connections beginning in January 1991.

2. The application has been protested by parties who are suing Del Oro in Superior Court challenging the main extension agreement on a number of grounds.

3. Del Oro acquired the water system in 1990 from the Lime Saddle Community Services District.

4. Del Oro's Lime Saddle District in 1990 served 259 customers in the community of Paradise in Butte County.

5. Because the district's five wells are inadequate to serve all customers, the district purchases water from the Stirling Bluffs Corporation and wheels it through the Paradise Irrigation District.

6. Stirling Bluffs and the irrigation district can terminate the purchased water agreement on five years' notice, and they can refuse to supply water if the needs of their own customers so require.

7. Because the source of water is interruptible, DHS has limited the number of additional connections that Lime Saddle can serve to 181.

8. To replace this interruptible source of water, Del Oro engineers designed an intertie project to take water from Lake Oroville, rights to which had been acquired from the Community Services District.

9. Cost of the intertie project was estimated at $2.8 million.

10. To finance the intertie project, Del Oro on January 1, 1991, began charging $5,000 for each new connection through a main extension agreement.

Conclusions of Law

1. The main extension agreement complies with Rule 15 of Del Oro's filed tariffs for its Lime Saddle District.

2. Based on a Commission audit of Lime Saddle District books, Del Oro has properly accounted for funds collected through the main extension agreements.

3. The categorization of this proceeding should be amended to state that hearings were required.

4. To promptly resolve this and the related superior court litigation, this order should be made effective immediately.

O R D E R

IT IS ORDERED that:

1. The application of the Del Oro Water Company requesting a determination to the effect that the main extension agreements required for new connections in Del Oro's Lime Saddle District comply with Del Oro's Tariff Rule 15 is granted.

2. The categorization of this proceeding is amended to show that hearings were required.

This proceeding is closed.

This order is effective today.

Dated _____, at San Francisco, California.